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28 January 1974

MEMORANDUM FOR: Mr. George Bennsky, State
Mr. Robert Ebel, Interior
Mr. Ben Huberman, NSC Staff

SUBJECT : Explanations and Evaluations of Alternative Plans for Sharing Oil in Emergencies

1. In response to your request for background information on oil sharing 25X1 we have prepared the attached report.

2. We would be pleased to provide any further analyses you may require.

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State Dept. review completed

DOE review completed.

Chief
Systems Development Staff
Office of Economic Research

Attachment:
Explanations and Evaluations of Alternative Plans for Sharing Oil in Emergencies

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Annex

EXPLANATIONS AND EVALUATIONS OF ALTERNATIVE PLANS FOR SHARING OIL IN EMERGENCIES

Overview

Each of the seven plans[1/] considered in 1973 by the Informal Group on Sharing of the OECD Oil Committee could affect oil prices and trade flows. The plans differ only in how oil supplies are to be allocated during crises. To the extent that any sharing plan succeeds, oil prices during an emergency would not be increased by a scramble for available supplies.

In comparing the plans against the alternative of no agreement on sharing, we omit price effects and political considerations, and focus only on differences in allocations during emergencies. Table 1 provides a brief explanation and evaluation of each plan. In subsequent sections and

1/ The plans are stated in the report Apportionment of Oil Supplies in an Emergency Among the OECD Member Countries (Paris, 19 November 1973). Distribution of the report was limited to the High Level Group of the OECD Oil Committee.

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Table 1

Summary Explanations and Evaluations of
Alternative Plans for Sharing Oil in Emergencies 1/

Plan Name	Description	Advantages to the US	Disadvantages to the US
Vital Needs	A complex plan proposed by French delegates to the Informal Group.	Parameters of the plan could in principle be adjusted so that during virtually all crises we could import more oil with the agreement than without it.	The parameters proposed by the French imply that their oil imports are much more important than ours. Under this assumption, the US would fare much better without an agreement to share.
Consumption-Based Sharing	During a crisis, each partner country takes an equal percentage cut in oil consumption.	During certain crises, we could import more oil with the agreement than without it.	In some cases we might be required to forgo all oil imports. In most embargoes directed not just against the US, we could import more oil under no agreement to share.
Consumption-Based Sharing, with Bonuses for Domestic Production	This plan is essentially undefined. The Group noted that in some cases it would be almost impossible to specify what the bonus would be, and who would get it.	Unknown.	Unknown.
Import-Based Sharing	During a crisis, each partner country takes an equal percentage cut in oil imports.	In all crises, this plan would allow us to import more oil than would consumption-based sharing. During the most likely embargoes, we would fare better under import-based sharing than under no agreement.	In relation to potential US cuts in oil consumption implied by import-based sharing, the corresponding cuts for Western Europe and Japan could well be so harsh that these nations would not adhere to the agreement.

1/ The plans are considered in the order listed in the Informal Group's report, ibid.

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Table 1 (continued)

Plan Name	Description	Advantages to the US	Disadvantages to the US
Arithmetic Compromise Between Import-Based Sharing and Consumption-Based Sharing	Import-based sharing implies one set of shares during a crisis, and consumption-based sharing implies another set of shares. An arithmetic compromise is simply a weighted average of the two alternative solutions.	To the extent that the import-based solution is weighted heavily, we would do well.	To the extent that the consumption-based solution is weighted heavily, we could import more oil under no agreement to share.
Combination of Import-Based Sharing, Essential Needs Sharing, and Consumption-Based Sharing	The paritcular combination suggested in the Group's report differs negligibly from consumption-based sharing.	If import-based sharing were weighted much more heavily in the combination, then the plan might be preferable to no agreement.	The combination suggested in the Group's report has essentially the disadvantages of consumption-based sharing.
Sharing on an Import Basis, but with a Limit on Differences in Percentage Cuts in Consumption	When the limit is zero, all partner countries take the same percentage cut in consumption, so in this case the plan reduces to consumption-based sharing. With a limit of 100 percentage points, the plan becomes import-based sharing. Between these extremes, the limit makes import-based sharing more acceptable to Western Europe and Japan.	Introduction of a limit on consumption cuts makes conceivable an import-based agreement with Western Europe and Japan.	If the limit is less than five percentage points, the agreement has the disadvantages of consumption-based sharing.

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and tables, the plans are illustrated in detail with numerical examples. Finally, the effects of seven plans in different possible crises are presented.

Numerical Examples

Six of the seven plans are illustrated in the order listed in the Group's report. One plan, namely consumption-based sharing with bonuses for domestic production, is not illustrated because the Group noted that in some cases it would be almost impossible to specify what the bonuses would be and who would get them.

The Vital-Needs Plan

We illustrate this plan with three examples in table 2. In all cases the plan transforms an initial set of losses--shown in the first column of each table--into a final solution shown in the last column of each table. The plan transforms the initial position differently depending on whether a crisis is severe, moderate, or mild. Example I illustrates a severe crisis defined as a case where priority needs exceed available supplies:

Table 2

Example I

Vital Needs Shares During an All-Arab Boycott of the US and Western Europe in 1975
(All quantities in millions of barrels per day unless otherwise stated)

	(1) Initial Loss	(2) Oil Consumption	(3) Priority Factors	(4) Priority Needs	(5) Oil Available	(6) Shares of Total Priority	(7) Distribution of Total Available Oil	(8) Loss After Distribution
United States	3.4	19.0	61.0%	11.6	15.6	39.7%	11.1	7.9
Western Europe	11.2	17.0	72.1%	12.2	5.8	41.7%	11.7	5.3
Japan	0.0	6.6	81.5%	5.4	6.6	18.5%	5.2	1.4
Total	14.6	42.6		29.2	28.0		28.0	14.6

Example II

Vital Needs Shares During an Iran/Iraq Cut-off of the US, Western Europe, and Japan in 1975

	(1) Initial Loss	(2) Oil Consumption	(3) Priority Factors	(4) Priority Needs	(5) Non-Priority Needs	(6) Priority Loss	(7) Excess Over Priority Needs	(8) Allocation of Loss	(9) Loss After Adjustment	(10) Loss Distributed by Non-Priority Needs	(11) Loss After Adjustment
United States	1.1	19.0	61.0%	11.6	7.4		6.3	1.1	2.2	3.92	3.06
Western Europe	3.5	17.0	72.1%	12.2	4.8		1.3	.2	3.7	2.54	3.12
Japan	2.5	6.6	81.5%	5.4	1.2	-1.3	0.0	-1.3	1.2	.64	.92
Total	7.1	42.6		29.2	13.4		7.6	0.0	7.1	7.10	7.10

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Table 2 (continued)

Example III

All Arab Embargo of the US Alone in 1975
(All quantities in millions of barrels per day unless otherwise stated.)

	(1) Initial Loss	(2) Oil Consumption	(3) Priority Factors	(4) Priority Needs	(5) Non-Priority Needs	(6) Allocation of Loss by Non-Priority Needs	(7) Loss Adjustments		(8) Loss After Adjustment
United States	3.4	19.0	61.0%	11.6	7.4	1.9	1.7	.95	2.65
Western Europe	0.0	17.0	72.1%	12.2	4.8	1.2	0.0	.60	.60
Japan	0.0	6.6	81.5%	5.4	1.2	.3	0.0	.15	.15
Total	3.4	42.6		29.2	13.4	3.4	1.7	1.70	3.40

Example IIIa

All Arab Embargo of the US Alone in 1975

	(1) Initial Loss	(2) Oil Consumption	(3) Priority Factors	(4) Priority Needs	(5) Non-Priority Needs	(6) Allocation of Loss by Non-Priority Needs	(7) Loss Adjustments		(8) Loss Adjustment
United States	3.4	19.0	61.0%	11.6	7.4	1.9	2.89	.285	3.175
Western Europe	0.0	17.0	72.1%	12.2	4.8	1.2	0.00	.180	.180
Japan	0.0	6.6	81.5%	5.4	1.2	.3	0.00	.045	.045
Total	3.4	42.6		29.2	13.4	3.4	2.89	.510	3.400

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-- columns (1) and (2) are initial losses and levels of consumption;

-- column (3) lists priority factors suggested by the French;

-- priority needs in column (4) come from multiplying each item in (2) times the corresponding priority factor in (3);

-- available oil supplies in column (5) are (2) minus (1);

-- percentage shares of total priority in column (6) are derived by dividing the total of (4) into each element of (4);

-- the shares of total available oil in column (7) are the total of (5) times the percentages in (6); and

-- The final solutions in column (8) are derived by subtracting the oil available in (7) from the oil consumption figures in (2).

A moderate crisis occurs when enough oil is available to meet total priority needs, but at least one partner's initial loss exceeds his non-priority needs. Computations in the moderate crisis illustrated by Example II are:

-- priority needs in column (4) are derived by multiplying each priority factor in (3) by the corresponding level of consumption in (2);

-- non-priority needs in column (5) are (2) minus (4);

-- a priority loss in column (6) is any negative value obtained by subtracting (1) from (5);

-- excesses over priority needs in column (7) are positive values obtained by subtracting (1) from (5);

-- the total shortfall in priority needs, which is the sum of column (6), is allocated in (8) by dividing the total of (7) into each element of (7), and then multiplying the results by the priority loss--in this case Japan's loss-- shown in(6);

-- the losses after adjustment in column (9) are (1) plus (8);

-- the losses are also distributed by priority needs in column (10), by dividing the total of (1) by the total of (5), and then by multiplying this result by each element in (5); and

-- the losses after adjustment in column (11) are one half the sum of (9) and (10).

Example III illustrates a mild crisis, in which each partner's priority needs would be met under the pattern of initial losses:

-- column (4) is (2) times (3);

-- column (5) is (2) minus (4);

-- column (6) is the total of (1) divided by the total of (5), multiplied by each element in (5);

-- the first loss adjustment column under (7) is .5 times (1), and the second loss-adjustment is .5 times (6), where the two values of .5 serve as weights for columns (6) and (7), and where another pair of weights such as .9 and .1 could be used; and

-- the loss after adjustment in column (8) is the sum of the adjustments in column (7).

Example IIIa shows how the solution in Example III would change if in computing loss adjustments under (7) we were to weight the initial solution in (1) by a factor of .85, and the solution in (6) by a factor of .15.

In summary, the outcome of the vital needs plan depends on:

-- the initial pattern of losses;

-- the priority factors; and

-- the weights used in computing loss adjustment.

Consumption-Based Sharing and Import-Based Sharing

The next table illustrates two plans, namely consumption-based sharing and import-based sharing. Columns (1), (2), (3), (4), and (5) apply in both cases.

-- column (1) lists normal imports, and (2) lists each bloc's share of total imports;

-- column (3) lists normal consumption, and (4) lists each bloc's share of total consumption; and

-- column (5) lists the loss in imports that each bloc experiences six months after the start of the crisis.

Under consumption-based sharing, each partner takes the same percentage cut in consumption:

-- the losses in consumption in column (9) are derived by multiplying each percentage in (4) times the total of (5); and

Table 3

Import-based Sharing and Consumption-based Sharing Under a Total Arab Embargo of the U.S. and a Five Percent Reduction Per Month in Arab Exports to Western Europe and Japan After 1 November 1973

(All quantities in millions of barrels per day unless otherwise stated.)

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
	Normal Oil Flows					Import Sharing			Consumption Sharing		
	Imports	Percent of total Imports	Consumption	Percent of Total Consumption	Loss Per Day After 6 Months	Loss in Imports	Imports	Consumption	Loss in Consumption	Imports	Consumption
United States	6.5	23.7	17.5	45.1	1.8	1.7	4.8	15.8	3.3	3.2	14.2
Western Europe	15.3	55.8	15.7	40.1	4.2	4.1	11.2	11.6	3.0	12.3	12.7
Japan	5.6	20.4	5.6	14.4	1.3	1.5	4.1	4.1	1.0	4.6	4.6
Total					7.3	7.3			7.3		

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-- the levels of consumption implied by the plan, namely values in column (11), are derived by subtracting (9) from (3).

Under import-based sharing, each partner takes an equal percentage cut in imports:

-- the losses in column (6) are derived by multiplying each percentage in (2) by the total of (5);

-- the imports after sharing, in column (7), result from subtracting (6) from (1); and

-- levels of consumption after sharing, in column (8), are derived by subtracting (6) from (3).

An Arithmetic Mixing of Oil Consumption Sharing and Oil Import Sharing

During any crisis, import-based sharing dictates one set of shares of available imports (as in column (7) of table 3), and consumption-based sharing dictates another set of shares of imports (as in column (10) of table 3). To compromise between these two plans, we could weight the import-based solution by 50%, and the consumption-based solution by 50%. Mechanically, this would amount to:

-- multiplying each import level in columns (7) and (10) of table 3 by .5, thereby getting two new columns, with the first number in each pertaining to the US, the second to Western Europe, etc.; and

-- adding the corresponding elements of each new column in order to get a third new column, namely the imports resulting from the 50/50 compromise.

The weights need not be 50% and 50%. The import-based shares could be weighted by 90% (e.g., by multiplying .9 times each element in column (7) of table 3), and the

consumption-based shares could be weighted by 10%. Any pair of positive percentages that add to 100% could serve as weights.

A Combination of Import Sharing, Essential Needs Sharing, and Oil Consumption Sharing

This combined plan consists of three distinct options for sharing, namely sharing on the basis of imports, of consumption, and of vital needs. Each of the three is explained above in this annex.

To determine which of the three would apply in a particular crisis, we examine the loss each partner country would suffer under an agreement to share on the basis of imports.

By definition, a mild crisis obtains when under an import-based agreement each partner suffers less than a 10% cut in consumption. During a mild crisis, the combined plan reduces to import-based sharing. Table 4 illustrates this in a particular case:

-- column (1) shows initial losses;

-- columns (2) and (3) show pre-crisis levels of consumption and imports; and

Table 4

Sample Applications of a Combination of Import Sharing, Essential Needs Sharing, and Oil Consumption Sharing
(All quantities are in millions of barrels per day unless stated otherwise.)

	(1) Initial Losses	(2) Pre-crisis Consumption	(3) Pre-crisis Imports	(4) Percentages of Total Imports	(5) Percentages of Total Consumption	(6) Essential Needs	(7) Import-based Consumption Levels	(8) Consumption Levels During Crisis
Example I--A Mild Crisis								
United States	1.0	17.5	6.5	24		15.75	17.05	17.05
Western Europe	.5	15.7	15.3	56	Not	14.13	14.64	14.64
Japan	.4	5.6	5.6	20	Applicable	5.04	5.21	5.21
Example II--A Moderate Crisis								
United States	1.8	17.5	6.5	24		15.75	16.60	15.83
Western Europe	1.1	15.7	15.3	56	Not	14.13	13.58	14.13
Japan	.9	5.6	5.6	20	Applicable	5.04	4.82	5.04
						34.92	35.00	
Example III--A Severe Crisis								
United States	1.8	17.5			45	15.75	15.8	14.2
Western Europe	4.2	15.7	Not	Not	41	14.13	11.6	12.7
Japan	1.3	5.6	Applicable	Applicable	14	5.04	4.1	4.6

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-- percentages in column (4) are derived by dividing the total of (3) into each element of (3).

Given the information in columns (1) - (4), we proceed to compute values for columns (6) and (7):

-- column (6) is derived by multiplying an arbitrary factor, in this case .9, times each element in (2), such that the results are "essential needs" for each partner; and

-- column (7) is derived by multiplying each percentage in (4) times the total of losses in (1), in order to distribute the total loss over partners, and then by subtracting the losses from consumption levels in (2).

Since in the first example of table 4 each essential need in column (6) is less than the corresponding level of consumption in column (7), then the crisis is mild and the final solution is sharing on the basis of imports, as in column (8).

In the second example we proceed exactly as in the first example in order to calculate essential needs in column (6) and import-based consumption levels in column (7). In this case, the essential needs of Western Europe and Japan are not met under import-based sharing, although the partners' total consumption exceeds their total vital needs. Thus by definition the crisis is moderate. In all moderate crises, the import-based solution in column (7) is adjusted so that all partners' essential needs are met, as in column (8).

In the third example we proceed as in the first two to compute columns (6) and (7). In this case the total essential needs exceed the total level of consumption possible during the crisis, so the crisis is termed severe. In all severe crisis, oil is allocated on the basis of consumption, as shown in column (8).

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Sharing on an Import Basis, but with Limits on Cuts in Consumption

Under consumption-based sharing, all partners always take equal percentage cuts in consumption, while under import-based sharing the partners do not. To share on an import basis, but to limit the disparity of percentage cuts in consumption, we begin with three arrays of numbers, namely the initial losses, the pre-crisis levels of consumption, and the pre-crisis imports, as in columns (1), (2), and (3) of table 5.

From these arrays we compute import-based consumption levels and consumption-based consumption levels, as explained above in this annex, and as illustrated in columns (4) and (5) of table 5. We then multiply each import-based level by .99, and each consumption-based level by (1-.99), or .01. These multiplications yield two sets of levels, namely the import-based levels weighted by .99, and the consumption-based levels weighted by .01. We add corresponding elements of the two sets to get a single compromise solution. In this case, the compromise is heavily biased toward the import-based solution.

Table 5

An Example of Sharing on an Import Basis, but with Limits on Cuts in Consumption
(All quantities in millions of barrels per day unless otherwise stated.)

	(1) Losses Under No Sharing	(2) Pre-Crisis Consumption	(3) Pre-Crisis Imports	(4) Import-based Consumption Levels	(5) Consumption-based Consumption Levels	(6) Weighted Solution for Consumption Levels*	(7) Weighted Solution for Consumption Levels**
United States	1.8	17.5	6.5	15.77	14.21	15.60	14.66
Western Europe	4.2	15.7	15.3	11.62	12.75	11.75	12.42
Japan	1.3	5.6	5.6	4.11	4.55	4.16	4.42

* No partner's percentage cut in consumption exceeds another's cut by more than 15 percentage points.

** No partner's percentage cut in consumption exceeds another's cut by more than five percentage points.

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The compromise implies a set of percentage cuts in consumption, one for each partner country. There may be great disparities among the percentage cuts in consumption. If we want to insure that no partner's percentage cut in consumption exceeds another's by more than 15 percentage points, we calculate a new compromise. In this case the import-based solution is weighted by .98 rather than .99, and the consumption-based solution is weighted by .02 rather than .01. If the compromise obtained by adding the two weighted solutions satisfies the condition that no percentage cut should exceed another by more than 15 points, then the compromise is final.

If the 15-point condition is not satisfied, we again revise the weights, this time to values of .97 and .03. We then compute a new compromise based on these weights, and determine whether the new solution meets the 15-point condition. If so, the compromise is final; and if not, we choose new weights of .96 and .04. Again we compute a compromise and then test it against the 15-point limit. We continue this process until the limit is just satisfied (see the solution in column (6) of table 5).

The same procedure applies for any agreed limit on the disparity of percentage cuts in consumption. The smaller the allowable disparity, the closer to consumption-based sharing will be the final solution (see column (7) of table 5).

Sample Effects of Alternative Sharing Plans Under Different Crises

Each of the six sharing plans illustrated above implies different shares in different crises. Samples of these different effects appear in tables 6 and 7.

Table 6
Allocations of Available Oil Under Alternative Criteria for Sharing

(Millions of Barrels Per Day)

1975		Normal Oil Flows		Libyan Embargo of US Only		Saudi Production Limited to 8.5 Million B/D		Libyan Embargo of US & Western Europe		All Arab Embargo of US, Japan & Western Europe	
		Imports	Consumption	Imports	Consumption	Imports	Consumption	Imports	Consumption	Imports	Consumption
Consumption Sharing	United States	8.0	19.0	7.9	18.9	7.7	18.7	6.8	17.8	0.2	11.2
	Western Europe	16.0	17.0	15.9	16.9	15.8	16.8	15.0	16.0	9.1	10.1
	Japan	6.6	6.6	6.6	6.6	6.5	6.5	6.2	6.2	3.9	3.9
Import Sharing	United States	8.0	19.0	7.9	18.9	7.8	18.8	7.3	18.3	3.5	14.5
	Western Europe	16.0	17.0	15.9	16.9	15.7	16.7	14.7	15.7	6.9	7.9
	Japan	6.6	6.6	6.6	6.6	6.5	6.5	6.0	6.0	2.8	2.8
Vital Needs Sharing I*	United States	8.0	19.0	7.85	18.85	7.8	18.8	7.2	18.2	0	11.0
	Western Europe	16.0	17.0	15.95	16.95	15.7	16.7	14.3	15.3	8.8	9.8
	Japan	6.6	6.6	6.6	6.6	6.5	6.5	6.5	6.5	4.4	4.4
Vital Needs Sharing II*	United States	8.0	19.0	7.85	18.85	7.8	18.8	7.2	18.2	0	11.0
	Western Europe	16.0	17.0	15.95	16.95	15.7	16.7	14.3	15.3	8.8	9.8
	Japan	6.6	6.6	6.6	6.6	6.5	6.5	6.5	6.5	4.4	4.4
No Sharing	United States	8.0	19.0	7.8	18.8	7.8	18.8	7.8	18.8	4.6	15.6
	Western Europe	16.0	17.0	16.0	17.0	15.7	16.7	13.6	14.6	4.8	5.8
	Japan	6.6	6.6	6.6	6.6	6.5	6.5	6.6	6.6	3.8	3.8
Combination of Import Sharing, Essential Needs Sharing, and Oil Consumption Sharing	United States	8.0	19.0	7.9	18.9	7.8	18.8	7.3	18.3	.2	11.2
	Western Europe	16.0	17.0	15.9	16.9	15.7	16.7	14.7	15.7	9.1	10.1
	Japan	6.6	6.6	6.6	6.6	6.5	6.5	6.0	6.0	3.9	3.9
Limits on Cuts in Consumption**	United States	8.0	19.0	7.9	18.9	7.8	18.8	7.3	18.3	1.0	12.0
	Western Europe	16.0	17.0	15.9	16.9	15.7	16.7	14.7	15.7	8.7	9.7
	Japan	6.6	6.6	6.6	6.6	6.5	6.5	6.0	6.0	3.5	3.5

* On the basis of our understanding of the French position as presented in the paper Schéma de Répartition des Importations de Pétrole Brut of the Ministry of Industrial and Scientific Development. Vital Needs Sharing II is the same as Vital Needs Sharing I except that the US share of private transport considered vital is raised from 50% to 85%.

** Import sharing used as a basic scheme, and no bloc's consumption cut is 10% greater than the cut of another bloc.

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Table 7
Allocations of Available Oil Under Alternative Criteria for Sharing
(Millions of Barrels Per Day)

Option/Block		1973 Normal Oil Flows: Imports	1973 Normal Oil Flows: Consumption	1973 A Hypothetical Scenario Evaluated After Six Months*: Imports After Sharing	1973 A Hypothetical Scenario Evaluated After Six Months*: Consumption After Sharing
Oil Consumption Sharing	United States	6.5	17.5	3.2	14.2
	Western Europe	15.3	15.7	12.3	12.7
	Japan	5.6	5.6	4.6	4.6
Oil Import Sharing	United States	6.5	17.5	4.8	15.8
	Western Europe	15.3	15.7	11.2	11.6
	Japan	5.6	5.6	4.1	4.1
Vital Needs Sharing	United States	6.5	17.5	3.4	14.4
	Western Europe	15.3	15.7	11.9	12.3
	Japan	5.6	5.6	4.8	4.8
Combination of Import Sharing, Essential Needs Sharing, and Oil Consumption Sharing	United States	6.5	17.5	3.2	14.2
	Western Europe	15.3	15.7	12.3	12.7
	Japan	5.6	5.6	4.6	4.6
Limits on Cuts in Consumption**	United States	6.5	17.5	4.8	15.8
	Western Europe	15.3	15.7	11.2	11.6
	Japan	5.6	5.6	4.1	4.1

* The Hypothetical Scenario is a total Arab embargo of the United States, and a 5 percent reduction per month in Arab exports to Western Europe and Japan after 1 November 1973.

** Import sharing used as a basic scheme, and no bloc's consumption cut is 20% greater than the cut of another bloc.

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